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In the Supreme Court of the United States

OCTOBER TERM, 1946

No. 555

ELSIE C. EMERY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 28–40) is reported in 5 T. C. 1006. The opinion of the circuit court of appeals (R. 119–124) is reported ported in 156 F. 2d 728.

JURISDICTION

The judgment of the circuit court of appeals was entered on July 22, 1946 (R. 124). A petition for rehearing, filed on August 5, 1946, was denied on August 26, 1946 (R. 124). The petition for a writ of certiorari was filed on September 30, 1946. The jurisdiction of this Court is invoked under

Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the entire income of certain trusts created by her husband in 1937 is includible in the gross income of the taxpayer for the years 1939, 1940 and 1941, under Section 22 (a) of the Internal Revenue Code, where the taxpayer possessed the power to alter, amend or cancel the trusts at any time and thereby to receive the whole or any part of the principal of the trusts and undistributed income, free of all trusts.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 13–15.

STATEMENT

The facts as stipulated (R. 53–115) and as found by the Tax Court (R. 30–36) may be summarized as follows:

Taxpayer is the wife of Allan C. Emery, and resides with her husband in Weymouth, Massachusetts. Her individual income tax returns for the calendar years 1939, 1940 and 1941 were filed with the Collector for the District of Massachusetts. (R. 30.)

On August 20, 1937, Allan C. Emery created five trusts, with the Boston Safe Deposit and Trust Company as the trustee. He retained no reversionary interest in the trusts and had no

power to alter, amend, or revoke. (R. 30–31, 55–61.)

Under each of the trusts, the taxpayer was to receive during her lifetime $300 a month, payable first out of income and thereafter out of principal, if necessary. The balance of the net income was payable to such religious, charitable or educational institutions or associations as the settlor and the taxpayer might designate.

Paragraph five of the trust instruments provided (R. 32, 58):

> 5. Should the net income from the principal of the trust fund prove insufficient at any time to meet and discharge the annuity obligation in Paragraph 1 hereof imposed, or if for any reason to be expressed at any time by the said Elsie Conant Emery, it should be her desire or wish that the trust in this indenture created be terminated, she is hereby vested with full power and authority to cancel or revoke this trust at any time in whole or in part by a writing to that effect addressed to the Trustee, and she is further vested with the power to amend or alter this trust in such manner and at such time or times as she may see fit. In the event of cancellation or revocation by the said Elsie Conant Emery, it shall be the duty of the Trustee forthwith to pay unto her the whole of the principal of the trust fund, or such part or amount thereof, as she may designate, together with any accrued and undistributed income, less

> the charges there against, free and discharged of all trusts.

In the event of the decease of the taxpayer without having exercised the full power of revocation or cancellation, given to her in paragraph five of the trust instruments, provision was made for further disposition of the remaining trust funds (R. 31–33).

Amendments to each of the trusts were made by the taxpayer in 1937, 1939, 1942, and 1944 (R. 31, 34, 62–75). By the amendment in 1944, the taxpayer released all power which she had to amend, alter, or revoke the trusts (R. 34, 75).

The total income of the five trusts for 1939 was $28,943.62, before any deduction for any distribution to beneficiaries. Of that amount, $10,943.62 was reported by the fiduciary as set aside for religious, charitable, and educational purposes and $18,000 was reported as taxable to the fiduciary. (R. 34.)

Taxpayer did not report in her return for the year 1939 any income as having been received from any of the five trusts. The Commissioner increased the income reported by adding thereto the above-mentioned amount of $28,943.62, representing the total income of the five trusts for 1939, and decreased the income thus determined by allowing an additional deduction for contributions of $4,341.55, applying the 15 percent limitation with respect to such contributions. (R. 34.)

The taxable income of the five trusts for 1940 was $25,837.52 before any deduction for any distribution to beneficiaries. The five fiduciary returns show a total of $7,837.52 as the amount distributable to beneficiaries, and a total of $18,000 as the net income (taxable to fiduciary). The individual income tax return filed by taxpayer for 1940 reported $7,837.53,[1] as received by her from the five trusts but the return did not include any portion (except apparently one cent) of the $18,000. The Commissioner increased the income reported by adding thereto the amount of $17,999.99, representing the difference between the above-mentioned amounts of $25,837.52 and $7,837.53. The Commissioner also allowed taxpayer an additional deduction for contributions in 1940 of $2,457.06. (R. 35.)

For the year 1940, the trustee of the five trusts paid taxpayer a total of $18,000 from the five trusts and made contributions to different organizations from the five trusts in the total amount of $1,075. The balance of the net income of the five trusts for the year 1940 was accumulated. (R. 35.)

The total income of the five trusts for 1941 was $44,949.46 before any deduction for any dis-

[1] This amount and the $26,177.01, similarly described for 1941 (see *infra*, p. 6), was, for some reason not explained in the record, thus reported, although taxpayer did not, in fact, receive it (R. 50). She makes no claim here with reference to these amounts. See Pet. 5–6.

tribution to beneficiaries. The five fiduciary returns show a total of $26,177.01, as the amount distributable to beneficiaries, and a total of $18,772.45 as the net income (taxable to fiduciary). The individual income tax return filed by taxpayer for 1941 reported $26,177.01 as received by her from the five trusts but did not include any portion of the $18,772.45. The Commissioner increased the income reported by adding thereto the amount of $18,772.45,[2] representing the difference between the above-mentioned amounts of $44,949.46 and $26,177.01. The Commissioner also allowed taxpayer an additional deduction for contributions in 1941 of $224.38. (R. 35–36.)

For the year 1941, the trustee of the five trusts paid taxpayer a total of $18,000 from the five trusts and made contributions to different organizations from the five trusts in the total amount of $2,455. The balance of the net income of the five trusts for the year 1941 was accumulated. (R. 36.)

Taxpayer's individual income tax returns for the years 1939, 1940 and 1941, were prepared on the basis of cash receipts and disbursements (R. 36).

Except for minor adjustments which are not involved on this appeal, the deficiencies in income tax asserted against the taxpayer are due to the Commissioner's determination that the net in-

[2] This amount of $18,772.45 includes $2.45 of a net long-term capital loss adjustment of $3.73 which is not involved on this appeal.

come as disclosed by the taxpayer's returns for the years 1939, 1940 and 1941 should be increased on account of "income from fiduciaries" of $28,943.62, $17,999.99 and $18,770, respectively. The Commissioner's determination that the entire income of the five trusts created by taxpayer's husband was taxable to the taxpayer was based upon the ground that the taxpayer had the power to amend or alter the trusts in such manner and at such time or times as she might see fit, and the power to cancel or revoke the trusts at any time or times in whole or in part and thereby to receive in her own right the principal of the trusts. (R. 12, 14, 29.) The Tax Court and the court below agreed with the Commissioner that the powers thus vested in the taxpayer required that the income of the trusts should be taxed to her under Section 22 (a) of the Internal Revenue Code. (R. 38–40, 119–124.)

ARGUMENT

1. The decision of the court below is in accord with a great wealth of authority in this Court, the circuit courts of appeals and the Tax Court. See *Helvering* v. *Clifford,* 309 U. S. 331; *Helvering* v. *Horst,* 311 U. S. 112; *Harrison* v. *Schaffner,* 312 U. S. 579; *Corliss* v. *Bowers,* 281 U. S. 376; *Richardson* v. *Commissioner,* 121 F. 2d 1 (C. C. A. 2d), certiorari denied, 314 U. S. 684, rehearing denied, 314 U. S. 714; *Jergens* v. *Commissioner,* 136 F. 2d 497 (C. C. A. 5th), certiorari denied,

320 U. S. 784; *Mallinckrodt* v. *Nunan,* 146 F. 2d 1 (C. C. A. 8th), certiorari denied, 324 U. S. 871, rehearing denied, 325 U. S. 892; *Frank* v. *Commissioner,* 145 F. 2d 413 (C. C. A. 3d); *Russell* v. *Commissioner,* 45 B. T. A. 397. See also *Richardson* v. *Commissioner,* 151 F. 2d 102 (C. C. A. 2d), certiorari denied, 326 U. S. 796.

The contentions made by the taxpayer in the petition for certiorari bear a marked similarity to the contentions advanced in the petitions for certiorari in the *Jergens, Mallinckrodt* and *Richardson* cases, *supra.* Since the denial of certiorari in those cases, nothing has occurred which would call for a review by this Court in the present case of the now well-settled principles which control here.

In the *Jergens* petition, as in the present petition (Pet. 7, 9–12), conflict was alleged with the decision of the Ninth Circuit Court of Appeals in *Commissioner* v. *Giannini,* 129 F. 2d 638. In the *Giannini* case a corporation had passed a resolution to pay the taxpayer there involved certain compensation for his services to the corporation, but the Board of Tax Appeals found that the taxpayer did not receive the money and did not direct its disposition when the corporation subsequently used the money to establish a Foundation of Agricultural Economics at the University of California. The circuit court of appeals rejected the Commissioner's contention that there was insufficient evidence to support the Board's finding

that the taxpayer had not directed the disposition of the money, stating (p. 641) that all the taxpayer did was to refuse unqualifiedly to accept any further compensation with the suggestion that the money be used for some worth while purpose. Indeed, it is doubtful that the court even passed upon the question whether a waiver of compensation, with nothing more, is such an exercise of dominion over the moneys to be received as to render them taxable, for, as pointed out in the footnote at page 641 of the opinion, the year in which the taxpayer renounced any further compensation was not before the court. But if it be assumed that the court did hold that a renunciation of a right to receive compensation for personal services would not result in the realization of income, that question is far removed from the question here presented.

In the present case, the income was derived from property. This property was subject to the complete and unfettered control of the taxpayer to do with as she might please. The only act required of her to secure the entire principal and income of the trusts in her own right, discharged of all trusts, was to address a writing to the trustee cancelling the trusts. Or, by alteration or amendment of the trusts, she could have directed the principal and income to be disposed of in any manner that might suit her fancy. The taxpayer accepted these incidents of ownership of the principal and income of the trusts and continued to

enjoy them during all of the taxable years, and it was not until the year 1944 that she divested herself of these rights. As stated by the court below (R. 122), a person could have a more unrestricted control of property only by having outright title and the act required to give the taxpayer outright title was so negligible that her position cannot be treated any differently from that of an outright owner.

The earlier decision of the court below in the case of *Plimpton* v. *Commissioner,* 135 F. 2d 482, which the taxpayer alleges (Pet. 7, 13) to be in conflict with that court's present decision is sufficiently distinguished in the court's opinion (R. 124).

2. The cases of *Burnet* v. *Whitehouse,* 283 U. S. 148, and *Helvering* v. *Pardee,* 290 U. S. 365, relied upon by the taxpayer (Pet. 14–15), are not inconsistent with the decision below. Those cases involved annuities which were a charge against principal as well as income, but the annuitants had no such powers as were possessed by the taxpayer in this case. The holding there was that the annuities were gifts and that the periodical payments were not a distribution of income but a discharge of the gifts and, as such, not taxable as income. Here the holding is that the taxpayer acquired substantial ownership of the entire principal of the trusts. Such principal constituted the gift to the taxpayer. While Section 22 (b)

(3) of the Internal Revenue Code (Appendix, *infra,* p. 13) provides that the value of property acquired by gift shall not be included in gross income, it further provides that the income from such property shall be included in gross income. The entire income from the trusts is taxed to the taxpayer, not because of her actual receipt of a portion of it, namely the $300 monthly payment from each of the trusts, but because of her substantial ownership of the entire principal of the trusts, which was the source of the income, and because of the complete control possessed by her over all of the income. The circumstance that she was to be paid a portion of the income under the trusts as they were originally drawn does not derogate from her complete control of the whole.

The case of *Helvering* v. *Grinnell,* 294 U. S. 153, cited by the taxpayer (Pet. 14–15), involved an estate tax statute, which, in its then form, required that property "pass" under the exercise of a general power of appointment to be included in the decedent's estate. That case is irrelevant to the question here. And Section 167 (c) of the Internal Revenue Code, referred to by the taxpayer (Pet. 18–19), was added by the Revenue Act of 1943, Sec. 134, 58 Stat. 51, was not made generally retroactive, and applies, moreover, only to amounts distributable in satisfaction of a legal obligation to support or maintain.

CONCLUSION

The decision below is correct; there is no conflict of decisions; and there is no occasion for further review.

Respectfully submitted.

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OCTOBER 1946.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(b) *Exclusions from Gross Income.*—The following items shall not be included in gross income and shall be exempt from taxation under this chapter:

* * * * *

(3) *Gifts, bequests, and devises.*—The value of property acquired by gift, bequest, devise, or inheritance (but the income from such property shall be included in gross income);

* * * * *

(26 U. S. C. 22.)

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(o) *Charitable and Other Contributions.*—In the case of an individual, con-

tributions or gifts payment of which is made within the taxable year to or for the use of:

* * * * *

(2) a domestic corporation, or domestic trust, or domestic community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

* * * * * *

to an amount which in all the above cases combined does not exceed 15 per centum of the taxpayer's net income as computed without the benefit of this subsection. Such contributions or gifts shall be allowable as deductions only if verified under rules and regulations prescribed by the Commissioner, with the approval of the Secretary.

* * * * *

(26 U. S. C. 23.)

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

(a) There shall be allowed as a deduction (in lieu of the deduction for charitable, etc., contributions authorized by section 23 (o)) any part of the gross income, without limitation, which pursuant to the terms of the will or deed creating the trust, is during the taxable year paid or perma-

nently set aside for the purposes and in the manner specified in section 23 (o), or is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, or for the establishment, acquisition, maintenance or operation of a public cemetery not operated for profit;

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

* * * * *

(26 U. S. C. 162.)

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